

RIGA

MARKET STUDY

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Summary

Following document review the experience of establishing a renovation scheme in other countries. Main and most significant examples for Riga are experience of Estonia and Lithuania as they are most relevant considering country specifics.

Energy security and European practice on establishing municipal revolving funds

Despite European progress in the area of energy security, EU is still exposed to the risks of energy (price) shocks. Therefore, a strategy has been developed for the protection of the energy field, and it outlines specific short-term and long-term measures for securing stability in Europe and decreasing dependence on energy import. The energy security strategy is closely linked to the Europe 2030 climate and energy framework, providing for improved competitiveness, development of low-carbon economy and reduction of fossil energy import.

In the short time, EU needs to improve its preparedness for disruptions with regard to external energy supplies by strengthening the existing emergency and solidarity mechanisms through risk assessment (energy security stress testing) involving Member States, regulatory authorities, management system operators and the European Commission. Apart from that, there is a need of investment in infrastructure for improved energy efficiency, more comprehensive regulatory documents and a closer cooperation among EU Member States.

In the long term, the task is to have a better functioning and more integrated energy market with more grid connections internally and a broader redistribution network. For achieving better energy security and transition to low-carbon economy, it is important to provide for efficient use of the EU financial instruments for 2014-2020, i.e. structural funds, the funding from EIB and ERDB for the priority areas. Faster reactions and capability to deal with challenges requires a better coordinated energy policy of the EU Member States and closer cooperation in the context of information exchange.

The involvement of residents and interested parties in resolving energy efficiency issues plays a crucial role in reaching the aims set out in the Covenant of Mayors. By establishing a mechanism for stimulating local investment, significant results could be achieved in housing renovation which presently is in a low activity stage in Riga. A municipal revolving fund for housing renovation could serve as the mechanism for providing a long-term solution. In the ideal case the financing scheme should be structured in a way where investments would be recovered from the savings on energy costs and would be returned to the fund with no burden of debt resulting for the final beneficiaries. Thus, in the city of Delft (Netherlands),

there is a revolving fund which provides for loans with minimum interest to residents and non-profit organizations wishing to improve energy efficiency and reduce the amount of energy consumed within their house (or apartment). The revolving fund concept is based on the rule that the period for returning the loan is the same as the pay-back time of implemented energy measures (recovery of investment); thus, credit instalments return into the fund and provide for further re-financing possibilities of energy efficiency measures. Notably, however, same time the Delft Fund, firstly, is not based on the principle of a revolving fund, and, secondly, is not readily adaptable to the situation in Riga (given the differences in infrastructure, volumes and renovation required, etc.). The Delft Revolving Fund provides for loans at a rate of 1.5-4 % for a period of 10 years. The average loan is from 1 500 to 10 000 EUR for households and 1 500 – 50 000 EUR for NGOs, and does not require any guarantees or collateral. There are limitations on the monthly re-payment amounts. The administrative matters are handled by the bank (SVn), whereas the municipality takes care of the management of the Fund.

Similar revolving funds have been established by the neighbouring States of Latvia in the Baltic region.

Lithuanian experience

Lithuanian government institutions have supported energy efficiency improvements in multi-apartment residential buildings in a number of ways. Support was launched in 2006 by ensuring state budget grants of up to 50 % of the energy efficiency project costs of multi-apartment buildings. Although the programme was successful from the point of view of the owners of the buildings, the earmarked funds of the state budget had been utilized already by the end of 2007¹.

Loans

In view of the lessons learned in the framework of the EU funds' programming period 2007-2013, Lithuanian institutions introduced a support programme for energy efficiency measures in multi-apartment buildings through a finance instrument. In mid-2009, the

¹ Ex-ante assessment of financial accessibility for energy efficiency projects in multi-apartment buildings in Latvia for the EU funds' programming period 2014-2020. Ministry of Economics of Latvia, 2015, p. 48-49.

Lithuanian institutions signed a cooperation agreement with the European Investment Bank (hereafter EIB) on establishing an investment fund of 227 million EUR (127 million EUR coming from European Regional Development Fund and 100 million EUR – from the state budget) in the framework of the JESSICA (Joint European Support for Sustainable Investment in City Areas) special support instrument. The support mechanism provided for subsidized loans to the owners of multi-apartment housing units. To offer the support product on the market, JESSICA launched a public procurement tender for financial intermediaries (commercial banks), and established a separate urban development fund with each of them.

A fixed interest rate of 3 % with a 20 year repayment period was applied to the loan. The financial intermediaries could ask the apartment owners to make a down payment which did not exceed 5 % of the project amount.

As the programme was launched, the commercial banks concluded loan agreements with the owners of every individual apartment. There were authorized representatives who were responsible for concluding the agreements with the commercial bank (on behalf of the apartment owners), drafting the projects, procurement and project implementation. The contractual procedure envisaged individual repayment of the loan to the commercial bank by every apartment owner.

As this loan procedure proved to be very cumbersome, from July 2012 the authorized representatives were allowed to conclude loan agreements with the commercial bank on their own behalf, the apartment owners being indicated as the final beneficiaries. According to these arrangements, the authorized representative consolidated the monthly loan repayments of the apartment owners and made the base amount and loan interest payments to the commercial bank. The loan was tied to the apartment, and not its owner.

In 2013 there were amendments to the Lithuanian legislation, which could now offer an alternative option for implementing urban or regional-level energy efficiency projects. According to the new implementation arrangements, loan agreements with the commercial banks could be concluded not only by the apartment owners and their authorized representatives, but also by municipality institutions. The municipalities targeted the buildings with the lowest energy efficiency in their areas (two lists of buildings prioritized for energy efficiency measures were drafted in the project framework).

The first list was based on the following requirements:

- It could include buildings with a yearly heat energy consumption above 150 kWh/m²;
- The buildings could not represent cultural or historical monuments;
- The buildings had to be constructed before 1993.

The second list was based on less stringent criteria:

- The buildings entered for the programme needed to have at least 10 apartments;
- The heat energy consumption of the building had to be above the average heat consumption within the municipality;
- The consolidated debt of the apartment owners could not exceed 10 % of the amount of the issued bills.

When drafting the list of buildings, the municipalities assessed the impact of the heat energy savings of the renovated buildings on the district heating system and appointed a project administrator, which could be:

- The manager of the housing unit;
- A municipal non-profit organization;
- A municipal institution.

The project administrator, similarly to the representative authorized by the apartment owners, took care of the project implementation and loan repayment to the commercial bank

Grants

Apart from the low interest loans, the following state support was offered:

- A grant up to 100 % of the costs for preparatory work on the project and project management (financed from the state budget).
- A grant up to 40 % of the project costs for the energy efficiency achieved (for a 20 % energy efficiency gain, grants of 15 % of the loan value were covered from the EU funds; for energy savings of at least 40 %, there was an additional grant of 25 % from the CCFI funding).
- A grant for individuals with low income covering 100 % of the project costs (financed from the state budget).

Monitoring

Responsibility for project monitoring and control was shared by the commercial banks and the Housing and Energy Savings Agency (state agency “Būsto energijos taupymo agentūra”). The Agency, for example, provided for the visual inspection of the technical documents of the project and construction work. The Agency also handled the administration of the support components financed from the state budget. The rest of the tasks related to issuance of the loans and monitoring were carried out by the commercial banks.

Key conclusions

Combining loans and grants is of key importance. On the other hand, establishing investment funds and organizing a public procurement tender for financial intermediaries stands to be time-consuming: it took 1.5 years to launch the loan product on the market after the agreement with EIB on establishing the JESSICA investment fund was signed. Our Lithuanian colleagues had to convince the public through additional information activities that the loan would be a valid instrument of the support mechanism, since previously the programme support had been rendered through grants.

Estonian experience

In Estonia, support for increasing the energy efficiency of housing is provided by the Estonian State Credit and Export Guarantee Fund (hereafter, KredEx)².

Loans

In the EU funds’ programming period 2007-2013, the programme provided for loans from the banks, which were financed from the Revolving Fund. The contributions to the Fund consisted of:

ERDF financing amounting to 17.7 million EUR (25 % of the contributions to the Fund).

KredEx financing amounting to 9.5 million EUR (13% of the contributions to the Fund).

Council of Europe Development Bank (hereafter, CEB) loan amounting to 28.8 million EUR (40 % of the contributions to the Fund).

² Ex-ante assessment of financial accessibility for energy efficiency projects in multi-apartment buildings in Latvia for the EU funds’ programming period 2014-2020. Ministry of Economics of Latvia, 2015, p. 50-51.

Estonian government loan amounting to 16 million EUR (22 % of the contributions to the Fund).

Commercial banks did not invest their own resources into the loans. For launching the product on the market, KredEx contracted two commercial banks on the basis of a cooperation agreement without a public procurement tender procedure. The requirement for the apartment owners was to make a contribution of at least 15 % of the project amount. The source of the contribution could be a grant, the apartment owner's own resources or a commercial loan.

The rate of the loan was 3.5 % (starting with 2013) or 4.5 % (before 2013), and it was fixed for a period of 10 years (public resources for the commercial banks were available at a 2 % rate, and the rate added by the bank was 1.5-2.5 %). The programme provided for a repayment period for the loan of up to 20 years, but in practice the average repayment period was projected at 15 years.

In the framework of the project, the loan was available on condition that in buildings of up to 2 000 m² at least 20 % of heat energy savings should be secured, whereas in larger buildings the savings had to be at least 30 %. Another eligibility condition was that at least 50 % + 1 of the apartment owners had to vote in favour of the energy efficiency measures. The commercial banks did not require more stringent criteria for the voting.

The loan agreements were signed by apartment owners' associations who took responsibility for the project implementation and loan repayment, and organized the loan repayment for all the apartment owners. In total 660 loans were issued for works targeted at improving energy efficiency in multi-apartment houses.

Guarantees

Apart from the loan, there were also state budget and KredEx (seen as similar to state guarantees) guarantees for loans issued for improving energy efficiency, from 2002. The guarantees were applied in the cases when the bank project was considered to have a risk level above the market average: high debtor levels, low market value of real estate in the location of the multi-apartment house, significantly higher than average investment costs per square metre of the building qualified the project for a guarantee. The guarantees covered a maximum of 75 % of the loan amount, and were available at an annual payment

of 1.2 – 1.7 % of the remainder of the amount guaranteed. KredEx guarantees have been applied for a maximum of 25 % of the total number of loans issued.

Grants

Grants for energy efficiency projects covering 15 – 35 % of the renovation costs were financed from CCFI funding. The amount of the grant was set on the basis of the projected savings and the scale of the project (the bigger the scale of the project and the heat energy savings, the bigger the share covered by the grant):

- 15 % grant:
 - Minimum requirements for the loan fulfilled.
 - At least 20 % of heat energy savings in buildings up to 2000 m², or at least 30 % of heat energy savings in buildings above 2000 m².
 - E-class to be achieved with regard to energy consumption (energy consumption below 250 kWh/m²).
- 25 % grant:
 - Improvement of energy efficiency of the roof, façade, replacement of windows (U value 1.1), management of the heat-supply system within the project framework.
 - At least 40 % of heat energy savings secured.
 - D-class to be achieved with regard to energy consumption (energy consumption below 200 kWh/m²).
- 35 % grant:
 - Improvement of energy efficiency of the roof, façade, replacement of windows (U value 1.1), management of the heat-supply system, and installation of a ventilation system with recuperation within the project framework.
 - At least 50 % of heat energy savings secured.
 - C-class to be achieved with regard to energy consumption (energy consumption below 150 kWh/m²).

Monitoring

The commercial banks provide for the monitoring and control of the projects at their own discretion (when deciding on the loans and when issuing them). The commercial banks

are responsible for the compliance of the buildings and projects with the programme requirements. After the loan has been issued, KredEx conducts an inspection of 5 % randomly selected buildings supported in the programme. Data on energy savings achieved in the projects are collected and stored after implementation. If the performance indicators achieved are lower than projected, the amount of the grant is reduced.

Management of the housing units

One of the reasons for a lower credit risk margin on loans for energy efficiency measures is a sustainable ownership and management policy in the housing area in Estonia.

In the nineteen nineties, when residential housing in Estonia underwent privatization, the Estonian Government chose a management model focussing on associations of apartment owners.

Associations of apartment owners took over the management of multi-apartment housing units from the state (municipality) owned housing departments. According to the regulations of the Republic of Estonia, associations of apartment owners are going to be the only bodies authorized to run the housing units. The interests of apartment owners are represented by a professional association – the Estonian Housing Management Association, which in the course of its 18 years of existence has accumulated considerable experience in the area of housing management and renovation.

In parallel, the public sector of Estonia has made a targeted effort to enable the owners of multi-apartment buildings and their representative bodies to take care of the management and renovation of the multi-apartment housing units. The public sector support measures planned for the future are focused on enabling the apartment owner associations; for example, on establishing a system of certified project managers in renovation and energy efficiency in the EU funds' 2014-2020 programming period.

Due to the abovementioned reasons, there is no single ESCO company doing business in Estonia today. The owners of multi-apartment houses are used to handling housing management issues and energy efficiency measures themselves.

Key conclusions

Estonia considers its background experience positive and one that matches the present market situation. Following the loans that were issued in the 2007-2013 EU funds'



programming period, the commercial banks have satisfied themselves that loans for energy efficiency projects in multi-apartment housing units have a low risk, and they are ready to invest their own private resources into loans for apartment owners at favourable rates.

In addition, Estonian colleagues indicated the importance of combining loans and grants, and information to the public on the available support mechanisms.